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SUBJECT: GEORGIA: INVESTMENT CLIMATE STATEMENT 2009

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¶1. Per reftel, Embassy Tbilisi submits its Investment Climate Statement for Georgia for 2009.

Introduction

Since 2004 when the Saakashvili Government came to power, the Georgian Government has undertaken an ambitious program to modernize and liberalize its economy. Institutional reforms include the restructuring and downsizing of government ministries, the privatization of large state-owned entities, increasing the pay of public servants, reducing the number and rates of taxes, improving tax and fiscal administration, streamlining licensing requirements, simplifying customs and border formalities, and generally undertaking efforts to make it easier to do business in Georgia. The current Georgian leadership views liberal market economies like Singapore and Dubai as models for its economic growth policies. Georgia,s economy, which was on the path of steady double digit growth since early 2004, suffered a considerable shock due to the Russian invasion in 2008 and subsequent global credit crisis. Nevertheless, Georgia still managed to achieve modest GDP growth in 2008; it is unclear what the final numbers will be in 2009.

The World Bank recognized Georgia as the world,s fastest reforming economy in IFC,s 2007 &Doing Business8 report, and its 2008 report ranks it as the world,s 18th easiest place to do business, in league with countries such as Switzerland, Estonia and Belgium. Georgia is ranked ahead of France, Germany and the Netherlands. Georgia further improved its rating in IFC,s &Doing Business 20098 moving up from 18th to 15th place. For comparison, Russia ranks as 120, Kazakhstan 70, Azerbaijan 33, and Armenia 44.

The World Bank,s &Anti-Corruption in Transition 38 report places Georgia among the countries showing the most dramatic improvement in the fight against corruption, due to implementation of a strong program of economic and institutional reform. The report indicates that the amount of money companies spend on bribes fell substantially in the period covered. Reforms have increased tax revenues, facilitating public investment and social sector expenditure to address poverty. Electricity distribution has become much more reliable. Paying customers in most parts of Georgia can count on consistent 24-hour a day service, although service can still be a problem in some remote rural areas.

The World Bank/IFC "Doing Business - 2009" report provides objective measures of business regulations and their enforcement across 181 countries and is a guide for evaluating regulations that directly impact economic growth. In terms of the pace of economic reform over 2007, The World Bank ranks Georgia fifth after Egypt, Croatia, Ghana, and FYR

Macedonia.

Among the specifi achievements for which the IFC credited Georgia in the 2008 report were strengthening investor protections by amendments to its securities law that eliminate loopholes which had allowed corporate insiders to expropriate minority investors. Georgia adopted a new insolvency law that shortens timelines for reorganization of a distressed company or disposition of a debtor's assets. It sped up the approval process for construction permits and simplified procedures for registering property. It made starting a business easier by eliminating the paid-in capital requirement. In addition, the country's private credit bureau added payment information from retailers, utilities, and trade creditors to the data it collects and distributes.
Qand trade creditors to the data it collects and distributes.

IFC,s 2009 report singled out areas of Starting a Business, Registering Property, Getting Credit and Paying Taxes, as Georgia,s priority achievements in 2008. The report reads: &Georgia,s private credit bureau now distributes a full range of information, including on-time repayment patterns and outstanding loan amounts. Coverage increased 20-fold, and banks can now have a better understanding of the payment patterns of potential borrowers. In addition, new regulations guarantee the right of borrowers to inspect their data at the private credit bureau, helping to improve the quality and accuracy of credit information. Amendments to the civil code, effective in December 2007, address secured transactions, allowing parties to a security agreement to agree to out-of-court enforcement of the creditor,s security right at the time the parties sign the security agreement. The corporate income tax rate was reduced from 20 percent to 15 percent, and the social tax abolished. A new online business registry makes it easier to register property by eliminating the requirement for legal entities to obtain several pre-registration documents. This reform reduced the number of procedures required to transfer a title from five to two, and the time from five days to three. Registration fees were also reduced. Finally, amendments to the Law on Entrepreneurs made it easier to start a company by eliminating the requirements for a minimum capital, a company seal, and a company charter and by making the use of notaries optional.8

Georgia scored high in the Economic Freedom Report jointly undertaken by the Heritage Foundation and the Wall Street Journal. The 2008 Index of Economic Freedom measures 162 countries across 10 specific factors of economic freedom, such as Business Freedom, Trade Freedom, Fiscal Freedom, Freedom from Government, Monetary Freedom, Investment Freedom, Financial Freedom, Property Rights, Freedom from Corruption, and Labor Freedom. Georgia's economy is above average at 69.2 percent free (68.7 in 2007), which makes it the world's 32nd freest economy and qualifies under the category of 'moderately free', in the company of Spain, Austria, Norway, the Slovak Republic, and the Czech Republic. Georgia is ranked 18th out of 41 countries in the European region, and its overall score is equal to the European regional average. According to the report, Georgia scores high in business freedom, fiscal freedom, freedom from government, investment freedom and labor freedom, but needs improvement in the areas of property rights protection and corruption.

Prudent fiscal and monetary policies have supported a relatively stable macro-economic environment and permitted the government to pay attention to further reform. The economy grew by 9.3 percent in 2005, and 9.4 percent in 2006 despite economic sanctions imposed by Russia, traditionally Georgia,s most important export market. Growth in 2007 was 12,4 percent and 8.5 percent in the first half of 2008. However, due to the August conflict with Russia and ensuing global credit crisis, the overall estimated growth rate for 2008 is expected to be roughly 2 percent. Initial projections for 2009 GDP growth are around 2 percent. Annual inflation for 2006 was 8.8 percent. It increased in 2007 to 9.2 percent and increased again to 10 percent in 2008. The government is committed to keeping inflation at the 7 percent

rate in 2009.

The Georgian Lari strengthened from 1.7 to about 1.6 per U.S. dollar over the course of 2007, and further appreciated against the dollar to 1.4 to 1 in the summer of 2008. The lari subsequently dropped to 1.65 to 1 versus the dollar by the end of 2008, affected both by the Georgia-Russia war and the global credit crunch. Based on the economy,s overall performance and the Georgian government,s strong commitment to structural changes, Georgia received its first sovereign credit rating in late 2005 from Standard and Poor,s -- a B long term, and B short term rating. Standard & Poor's cut Georgia's outlook to stable from positive in the beginning of May 2008, citing worsening relations with Russia, but kept its rating at B . The rating agency put Georgia on CreditWatch on August 8, when fighting broke out in the Georgian separatist regions, but removed Georgia,s ratings from CreditWatch negative in September, 2008, citing the end of fighting with Russia over South Ossetia and the provision of foreign aid to Georgia. Currently Georgia,s long-term Qof foreign aid to Georgia. Currently Georgia,s long-term debt is rated B by S&P, and the outlook is now stable. Fellow ratings agency Fitch currently rates Georgia, which launched its debut $500 million Eurobond in spring 2008, as BB- with a stable outlook.

Despite the improvements in the economy, more than 25 percent of the population lives below the poverty line, and many people still rely on subsistence agriculture. Greater familiarity with western business practices and legalnorms is required. Physical infrastructure, such as the road network, saw considerable improvement over 2005-2008, although much remains to be done, especially in rural areas. Government has allocated USD 310 million (need USD equivalent) for road rehabilitation projects in 2009. Most natural gas for heating and electricity generation is imported. Rehabilitation of existing hydroelectric power plants and construction of new ones is gradually reducing Georgia's dependence on imported energy.

The main source of sustained future economic growth will be private investment, both domestic and foreign. The government,s challenge is to implement existing legislation, continue the fight against corruption, defuse tensions in the separatist regions and undertake new reforms, in order to increase investor confidence.

Georgia receives assistance from the United States, the European Union and a range of international institutions. U.S. assistance has focused on the goals of improving the rule of law, governance and the administration of government economic and financial institutions, improving critical physical infrastructure, enhancing private sector competitiveness and promoting the growth of a free market economy. In 2006, Georgia,s clear-cut commitment to reform earned it one of the first compacts with the U.S. Millennium Challenge Corporation, which has provided investments in infrastructure, tourism and agriculture.

After the August 2008 conflict with Russia, foreign donors committed USD 4.5 billion to help Georgia recover from direct and indirect war damage. According to the World Bank-led international needs assessment for Georgia, the major impact of the conflict was on the investment and consumer climate, which led to a sharp economic drop in FDI and GDP. With this in mind, the USG committed to a USD 1 billion assistance package for Georgia dedicated to repair its damaged infrastructure and help the Georgian economy recover from the economic shock from the reduction in FDI immediately following the August conflict.
President Saakashvili and his government have strengthened Georgia,s bilateral relations with many countries, reaching out to Ukraine, Turkey, Italy, Poland, Latvia, Lithuania, Estonia, Japan, Kazakhstan, the UK, Germany, the Netherlands, and of course, the United States. Georgia has a partnership agreement with the European Union, and an action plan for reform to allow a closer relationship. Georgia maintains the goal of eventual membership in the European Union. Georgia

is one of only fifteen countries in the world that benefit from GSP access to the EU market, allowing duty-free access for more than 7000 products. It is making an effort to harmonize its regulatory environment with international standards, particularly those established by the EU. Georgia enjoys duty-free trade with other former Soviet Union countries. It benefits from preferential trading relationship with the United States, Turkey, Canada, Switzerland and Japan. In 2007 Georgia signed a free trade agreement with Turkey and a Trade and Investment Framework Agreement and an Open Skies Agreement with the United States. Discussion of a free trade agreement with the European Union is under way.

Georgia is located at the crossroad between Europe and Asia. It is the shortest route from Central Asia to Europe, and could be a North-South Bridge between Turkey and the Russian Federation. Georgia has two deep-water ports on its Black Sea coast. Labor costs in Georgia are comparable to the Far East, while transit time for shipment of goods to Europe is far less. The new government has launched an extensive road rehabilitation project aimed at upgrading the road quality and constructing new facilities to improve communication infrastructure. The governments of Turkey, Azerbaijan and Georgia have agreed to construct a rail link from Kars, Turkey through Georgia to Baku, Azerbaijan. Freight from Europe will be able to be transported through Turkey to Baku via Tbilisi and then to Central Asia from Baku by ferry. Ongoing construction of a tunnel under the Bosporus at Istanbul means freight will soon be able to travel from Georgia directly into Europe. In addition, Georgia is improving its network of rail ferry connections with Black Qimproving its network of rail ferry connections with Black Sea countries, including Russia, Ukraine, Romania and Turkey, which will further increase transportation and trade turnover with these countries.

Georgia,s relations with its northern neighbor Russia have been problematic. In 2005 and 2006, Russia banned imports of Georgian agricultural products, mineral water and wine. At the time, Russia was the largest importer of those products. These restrictions continued into 2008. In September 2006, Russia cut all direct transport links with Georgia. Gazprom, the Russian gas monopoly, quadrupled the price of natural gas supplied to Georgia over two years. Despite these actions, the Georgian economy has continued to grow. Georgian businesses are actively seeking new markets for Georgian products and new sources of imports, especially in Ukraine, the Baltics and Central Europe. New supplies of natural gas from Azerbaijan and increased hydroelectric generating capacity are making Georgia less dependent on Russian energy sources. The return of normal trading relations with Russia could create significant opportunities for companies based in Georgia.

Openness to Foreign Investment

Georgia is extremely open to foreign investment and is eager to welcome new investors. The country is developing a regulatory framework intended to foster competition. Legislation governing foreign investment establishes favorable conditions, but not preferential treatment, for foreign investors. The Law on Promotion and Guarantees of Investment Activity protects foreign investors from subsequent legislation that alters the condition of their investments for a period of ten years.

The U.S.-Georgia Bilateral Investment Treaty, in force since 1994, guarantees U.S. investors national treatment or most favored nation treatment, whichever is better, in the establishment, operation and sale of their investments. Exceptions to national treatment may be made by Georgia for investments in maritime fisheries; air and maritime transport, and related activities; ownership of broadcast, common carrier, or aeronautical radio stations; communications satellites; government-supported loans, guarantees, and insurance; and landing of submarine cables.

Legislation governing foreign investment includes the Constitution, the Civil Code, the Tax Code, and the Customs Code. Other legislation includes the Law on Entrepreneurs, the Law on Promotion and Guarantees of Investment Activity, the Bankruptcy Law, the Law on Courts and General Jurisdiction, the Law on Limitation of Monopolistic Activity, the Accounting Law, and the Securities Market Law.

Georgia has negotiated 34 agreements for avoidance of double taxation, of which 22 have entered into force. The active agreements are with Uzbekistan, Azerbaijan, Ukraine, Romania, Bulgaria, Turkmenistan, Armenia, Kazakhstan, Iran, the Netherlands, Greece, Italy, Belgium, Lithuania, Latvia, United Kingdom, China, Austria, Poland, Czech Republic and Estonia. Until treaties with France and Germany enter into force, a similar agreement signed by the USSR governs the issue. An agreement with Russia was signed in 1999 and ratified by the Georgian parliament in 2000. It has not been ratified by the Russian Duma, but the Russian side regards it as an active agreement. Treaties with Germany, France, Denmark, Finland and Turkey have been ratified by Georgian parliament and are awaiting ratification by the respective countries in order to enter into force.

The legal framework governing ownership and privatization of property is established by the following acts: the Civil Code, the Law on Ownership of Agricultural Land, the Law on Private Ownership of Non-Agricultural Land, the Law on Management of State-Owned Non-Agricultural Land, and the Law on Privatization of State Property. Property rights in the extractive industries are governed by the Law on Concessions, the Law on Deposits and the Law on Oil and Gas. Intellectual property rights are protected under the Civil Code, and by the Law on Patents and Trademarks. Financial sector legislation includes the Law on Commercial Banks, the Law on National Banks and the Law on Insurance Activities.

Georgia does not screen foreign investment in the country, other than imposing a registration requirement and certain licensing requirements as outlined below. Foreign investors have participated in most of the major privatizations of state-owned property. Transparency of such privatizations has at times been an issue, however. No law specifically authorizes private firms to adopt articles of incorporation which limit or prohibit foreign investment.
Qwhich limit or prohibit foreign investment.

In 2005, registration of businesses was simplified. Paperwork and fees were reduced and processing time shortened to about 8)10 days from the submission of documents. All companies are required to register with the Ministry of Finance, providing founder's and firm principals' names, dates and places of birth, occupations and places of residence; incorporation documents; area of activity; and charter capital. This information is made public and any person may request and review such information. Business registration and tax registration are separate procedures handled by the same department within the Ministry of Finance.
The Government of Georgia has privatized most of the largest formerly state-owned enterprises in the country. A list of entities still available to be privatized can be found on the website www.privatization.ge. Information on investment conditions and opportunities can be obtained from the Georgia National Investment and Export Promotion Agency, e-mail: info@investingeorgia.org, www.investingeorgia.org. Further information is available at a website maintained by the American Chamber of Commerce in Georgia, www.investmentguide.ge.
In 2005, 84 percent of existing licensing requirements were eliminated and a &one stop shop8 for licenses was created. By law, the government has 30 days to make a decision, and if no reasonable ground for rejection is stated by the licensing authority within that time, the license or permit is deemed to be issued. Construction permits can be obtained within 90 days, according to research published by the European Union. Licenses are only required for activities that affect public health, national security and the financial sector.
Licensing currently is required in the following areas:

weapons and explosives production, narcotic, poisonous and pharmaceutical substances, exploration and exploitation of renewable or non-renewable substances, exploitation of natural resource deposits, establishment of casinos and gambling hoses and the organization of games and lotteries, banking, insurance, trading in securities, wireless communication services, and the establishment of radio and television channels. The law requires the state to retain a controlling interest in air traffic control, shipping traffic control, railroad control systems, defense and weapons industries, and nuclear energy. Only the state may issue currency, banknotes and certificates for goods made from precious metals, import narcotics for medical purposes, and produce control systems for the energy sector.

Conversion and Transfer Policies

Georgian law guarantees the right of an investor to convert and repatriate income after payment of all required taxes. The investor is also entitled to convert and repatriate any compensation received for expropriated property. Moreover, Georgia has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the IMF Articles of Agreement, with effect from December 20, 1996. IMF members accepting the obligations of Article VIII undertake to refrain from imposing restrictions on payments and transfers for current international transactions and from engaging in discriminatory currency arrangements or multiple currency practices without IMF approval. By accepting the obligations of Article VIII, Georgia gives confidence to the international community that it will pursue sound economic policies that will obviate the need to use restrictions on the making of payments and transfers for current international transactions.

Under the U.S.-Georgia Bilateral Investment Treaty, the Georgian government guarantees that all transfers relating to a covered investment by U.S. investors can be made freely and without delay into and out of Georgia.

Foreign investors have the right to hold foreign currency accounts with authorized local banks. The sole legal tender in Georgia is the Lari (GEL), which is traded on the Tbilisi Interbank Currency Exchange and in the foreign exchange bureau market. There is no difficulty in obtaining foreign exchange or significant delays in remitting funds overseas through normal channels. Several Georgian banks participate in the SWIFT and Western Union interbank communication networks. Businesses report that it takes a maximum of three days to transfer money abroad. There are no known plans to change remittance policies. Travelers must declare at the border currency and securities in their possession valued at more than GEL 30,000 (USD 18,750).

Expropriation and Compensation

The Georgian Constitution protects ownership rights, including ownership, acquisition, disposal or inheritance of Qincluding ownership, acquisition, disposal or inheritance of property. Foreign citizens living in Georgia possess rights and obligations equal to those of the citizens of Georgia. The Constitution allows restriction or revocation of property rights only in cases of extreme public necessity, and then only as directly allowed by law.

The Law on Procedures for Forfeiture of Property for Public Needs establishes the rules for expropriation domain in Georgia. The law allows expropriation for certain enumerated public needs. It provides a mechanism for valuation and payment of compensation, and for court review of the valuation at the option of any party. The Georgian law on investment allows expropriation of foreign investments only with appropriate compensation. Recent amendments to the expropriation law allow payment of compensation with property of equal value as well as money. Compensation includes all expenses associated with the valuation and delivery of expropriated property. Compensation must be paid without delay and must include both the value of the expropriated

property as well as the loss suffered by the foreign investor as a result of expropriation. The foreign investor has a right to review of an expropriation in a Georgian court. In 2007, Parliament passed a law generally prohibiting the government from contesting the privatization of real estate sold by the government before August 2007. The law is not applicable to certain enumerated properties.

The U.S.-Georgia Bilateral Investment Treaty permits expropriation of covered investments only for a public purpose, in a non-discriminatory manner, upon payment of prompt, adequate and effective compensation, and in accordance with due process of law and general principles of fair treatment.

Dispute Settlement

The Georgian investment law allows disputes between a foreign investor and a governmental body to be resolved in Georgian courts or at the International Center for the Settlement of Investment Disputes (ICSID), unless a different method of dispute settlement is agreed upon between the parties. If the dispute is not considered at ICSID, the foreign investor has the right to submit the dispute to any international arbitration body which has been set up by the United Nations Commission for International Trade Law (UNCITRAL) to resolve the dispute in accordance with the rules established under the arbitration and international agreement. Under the U.S.)Georgia Bilateral Investment Treaty, investors have additional rights.

Georgia is party to the International Convention on the Recognition and Enforcement of Foreign Arbitration Awards. As a result, the Government agrees to accept binding international arbitration of investment disputes between foreign investors and the state. The Ministry of Justice was designated in December 2005 to oversee the government,s interests in arbitrations between the state and private investors.

It is recommended that contracts between private parties include a provision for international arbitration of disputes because of deficienciesin the Georgian court system. Litigation can take excessively long periods of time. There is concern about the adequacy of training of judges and about their susceptibility to pressure from the government or other outside influences.

Performance Requirements and Incentives

Performance requirements are not a condition of establishing, maintaining or expanding an investment, but have been imposed on a case-by-case basis in some privatizations, for example, commitments to maintain employment levels or to make additional investments within a specified period of time. While many privatizations have proceeded smoothly and regularly, the current government has used non-fulfillment of performance requirements to justify rescinding privatizations and re-selling enterprises, usually for higher prices, sometimes to the benefit of other interested parties.

Most types of performance requirements are prohibited by the U.S.-Georgia Bilateral Investment Treaty.

The Government of Georgia does not offer incentives to foreign investors, but relies on the many improvements it has made in the overall business climate to attract them to invest in the country.

Right to Private Ownership and Establishment

Foreign and domestic private entities may freely establish, acquire, and dispose of interests in companies and business enterprises, and engage in all forms of remunerative activity. Some specific laws regulate business activity in the banking, agribusiness, energy, transport and tourism
Qthe banking, agribusiness, energy, transport and tourism
sectors. To the extent that public enterprises compete with

private enterprises, they do on the basis of equality.

Foreign individuals and companies may buy non-agricultural land in Georgia. Only Georgian citizens or companies may buy agricultural land in their own name, but even agricultural land can be purchased by forming a Georgian corporation that may be up to 100 percent foreign-owned.

Investors should exercise extreme caution in purchasing property in Abkhazia. Land for sale rightfully may belong to internally displaced persons forced to leave Abkhazia in the early 1990s and may have improperly been placed on the market by the de facto authorities in Abkhazia. The government of Georgia considers the sale of property in Abkhazia illegal under Georgian law and property could be reclaimed by original owners at a future date.

Protection of Property Rights

Secured interests in both real and personal property are recognized and recorded. However, deficiencies in the operation of the court system can hamper investors from realizing their rights in property offered as security. Foreign investors' interests have sometimes been harmed by biased court proceedings, and by legislation and decrees that clearly favor a Georgian entity or partner involved in the enterprise. Judicial reform has been identified as a top priority for the Georgian government since late 2005, but it will take some time for court and legal reforms to bear fruit. It is recommended that contracts between private parties include a provision for international arbitration of disputes.

Disputes over property rights made headlines in 2005-2007. These cases have tended to undermine confidence in the impartiality of the Georgian judicial system and rule of law, and by extension, Georgia,s investment climate. Both foreign and Georgian investors have expressed reservations about the competence, independence and impartiality of court decisions. In a few cases lower court decisions have changed control of property or of entire enterprises on questionable legal grounds or on the basis of forged documents. In some cases these decisions have been reversed by higher courts or government action, in others not.

Protection of Intellectual Property Rights

Georgia acceded to the WTO and the TRIPS agreement in 2000. In 2004, the Georgian parliament ratified the Rome Convention for Protection of the Rights of Performers, Producers of Phonograms and Broadcasting Organization, and the Lisbon Agreement on Denomination of Origin. In 2005, Georgia joined WIPO International Convention for the Protection of New Varieties of Plants. Georgia is a party to the Bern Convention, member of the two WIPO digital treaties) Copyright Treaty and Performance and Phonograms Treaty, the Hague Agreement, and Budapest Treaty Concerning the International Recognition of the Deposit of Microorganisms for the Purpose of Patent Procedures.

Six laws regulate intellectual property rights. These include: the Law on Patents, Law on Trademarks, Law on Copyrights and Neighboring Rights, Law on Appellation of Origin and Geographic Indication of Goods, Law on Topographies of Integrated Circuits, and Law on IP Related Border Measures. Georgian law now provides retroactive protection for works of literature, art and science or sound recordings for 50 years.

While Georgia has brought its legislation into line with international standards, enforcement remains problematic. Pirated video and audio recordings, electronic games and computer software are freely sold in Georgia. Use of unlicensed software in government offices and businesses is common. Internet service providers host websites loaded with unlicensed content. Responsibility for WTO compliance was recently been transferred to the Ministry of Economic Development, which still needs to develop its capacity in

this regard. The Customs Department is developing a new Intellectual Property Objects Register to assist in identification of counterfeit goods at the border. Nevertheless, IPR awareness in the Department is low and QNevertheless, IPR awareness in the Department is low and hampered by frequent personnel changes. Further clarification of responsibilities between the Ministry of Internal Affairs and the Ministry of Finance is needed, as the MOIA has authority over some types of property rights protection, and the Ministry of Finance over others. Judges and lawyers lack training in IPR issues. Georgia,s Patent and Trademark Agency needs greater familiarity with emerging technologies.

Transparency of Regulatory System

The Georgian government has made a commitment to greater transparency and simplicity of regulation. Laws and regulations are published in Georgian in the official gazette, the Legislative Messenger. The number of taxes has been reduced from twenty-two to six. The tax on corporate profits is 20 percent. The tax on personal income was set at a flat rate of 25 percent after a 2007 law increased the personal income tax and eliminated the employer-paid social tax on wages. The Value Added Tax is 18 percent. Despite the duel economic shocks of the August conflict and the credit crisis, the Government of Georgia further reduced the personal income tax rate from 25 percent to 20 percent and reduced the dividend income tax rate from 10 percent to 5 percent. Both reductions took effect on January 1, 2009. This new initiative is an acceleration of legally binding commitments, made earlier, to reduce the personal income tax rate to 15 percent by 2013 and to further reduce the dividend income tax rate to 0 percent by 2012. Legislation was passed earlier in 2008 setting zero dividend and capital gains tax rate with respect to publicly traded equities (defined as having free float in excess of 25 percent). There are excise taxes on cigarettes, alcohol, and fuel. Only three rates of import duties exist, zero, 5 percent and 12 percent, and nearly all goods, except for some agricultural products, are taxed at the zero rate.

The Georgian National Investment and Export Promotion Agency has established Business Information Centers in Tbilisi and other Georgian cities. These centers are intended to provide domestic and foreign businesses with a standard package of information relevant to doing business in Georgia, and specific information according to the needs of individual businesses. The Business Information Centers are also conducting an ongoing public-private dialog to facilitate communication between regulators and the business community.

International accounting standards became binding for joint stock companies in Georgia from January 1, 2000. For other institutions, such as banking institutions, insurance companies and companies operating in the field of insurance, as well as limited liability companies, limited partnerships, joint liability companies, and cooperatives the standards became binding on January 1, 2001. Private companies (excluding sole entrepreneurs, small businesses and non-commercial legal entities) are required to perform accounting and financial reporting in accordance with international accounting standards. Sole entrepreneurs, small businesses and non-commercial legal entities perform accounting and financial reporting following simplified interim standards approved by the Parliamentary Accounting Commission. Despite the legal requirement, the conversion to international accounting standards is going slowly, in part because many businesses have operated in the shadow economy, or maintained two sets of books. Qualified accounting personnel are in short supply.

Efficient Capital Markets and Portfolio Investment

The Georgian banking system is growing quickly. Currently, the banking system consists of regional small- and medium-sized banks, a handful of large banking institutions based in Tbilisi with branch networks, and three foreign

banks (American, Turkish, and Azerbaijani). In 2007, commercial bank assets grew by 70 percent and the profit of commercial banks grew by 65 percent. Total assets of the country,s 19 banks (13 of which have foreign capital) were $4.5 billion at the end of 2006, 45 percent of GDP.

Credit from commercial banks is available to foreign investors as well as domestic clients. Banks offer credit cards and a variety of loans including mortgage loans. In addition, the International Finance Corporation, European Qaddition, the International Finance Corporation, European Bank for Reconstruction and Development, the U.S. Overseas Private Investment Corporation, the Millennium Challenge Corporation and other international development agencies have a variety of lending programs that make credit available to large and small businesses in Georgia.

The limited number of foreign banks operating in Georgia reflects in part the small size of Georgia,s financial market. However, foreign investment in the sector is significant, accounting for 67.6 percent of total bank capital in 2007. In 2005, Russian, Kazakhstani, U.S., and German capital was invested in Georgian banks. In September 2006, the French bank Societe Generale acquired 60 percent of one of the leading Georgian banks, Bank Republic. In 2007, growing interest towards Georgia,s banking sector was demonstrated by the entrance of the British bank HSBC into Georgia. Dabi Group acquired Standard Bank.

Georgian banks have remained solvent during the current global credit crisis largely due to the mandated 13 percent central bank reserve requirement and conservative lending practices. The Georgian central bank relaxed the reserve requirement to 5 percent in the aftermath of the war and in response to the global credit crisis to try to inject liquidity into the market and spur new lending. The reserve requirement remains at 5 percent.

Domestic credit to the private sector rose by more than 70 percent in real terms during 2007. The law on commercial bank activities has been amended to improve the transparency of ownership and corporate governance of banks. In March 2006, the restriction under which one shareholder or a group of joint shareholders could hold no more than 25 percent of voting shares in a bank was abolished. A new law regulating the activity of microfinance organizations came into force in August 2006.

The National Securities Commission of Georgia regulates the securities market. All joint stock companies with more than 50 shareholders -- currently about 1800 companies in Georgia -- are required to submit annual, semi-annual and current reports prepared in accordance with internationally accepted accounting standards.

The small Georgian Stock Exchange was established with assistance from USAID in 1999. The stock market organizes public trading of securities and disseminates information on trading results and prices. The GSE has a Memorandum of Cooperation with the Thessaloniki Stock Exchange Center for harmonization of trading platforms. Shares of 82 companies were traded on the GSE in 2008, up from 57 in 2007). In 2008, the GSE executed 3,180 trades compared to 7,313 in 2007, with a total value of GEL 256.5 million (around $160.3 million) compared to GEL 97 million (around $54 million) in ¶2006.

No law or regulation authorizes private firms to adopt articles of incorporation or association that limit or prohibit foreign investment, participation, or control. &Cross-shareholder" or "stable-shareholder" arrangements are not used by private firms in Georgia. Georgian legislation does not protect private firms from takeovers. There are no regulations authorizing private firms to restrict foreign partners' investment activity or limit foreign partners' ability to gain control over domestic enterprises.

Political Violence

Georgia suffered considerable instability in the immediate post-Soviet period. After independence in 1991, civil war and separatist conflicts flared up in the areas of Abkhazia and South Ossetia. The status of each region remains unresolved and the central government does not have effective control over these areas. The United States supports the territorial integrity of Georgia within its internationally-recognized borders. In August 2008, tensions boiled over culminating in the brief war between Georgia and Russia. Russia proceeded to invade and occupy portions of undisputed Georgian territory and destroyed portions of vital infrastructure, cut the main east-west highway and blockaded the Georgian port of Poti. Nearly all the destroyed infrastructure has been repaired and commerce has returned to normal. While the separatist regions of South Ossetia and Abkhazia have declared independence, thus far, only Russia and Nicaragua have recognized them. Tensions still exist and reports of violence both inside the breakaway republics and near the administrative boundary lines are common, but other parts of Georgia, including Tbilisi, are not directly affected.

Corruption

Under President Saakashvili, Georgia has taken action to reduce corruption. Anti-corruption efforts have resulted in Qreduce corruption. Anti-corruption efforts have resulted in the arrests of former officials, the radical downsizing of state bureaucracies, effective crackdowns on smuggling and have contributed to an increase of about 50 percent in state revenue collections. The notoriously corrupt traffic police were completely disbanded in mid-2004.

Articles 332-342 of the Criminal Code criminalize bribery. Georgian legislation provides for civil forfeiture of undocumented assets from public officials who are charged with corruption offenses. Bribery is a criminal act under Georgian law, and Parliament recently accepted a package of constitutional amendments that make abuse of public office a criminal offense with a maximum penalty of fifteen years imprisonment and confiscation of property. Penalties for accepting a bribe start at 6 years in prison and can be up to 15 years depending on aggravating circumstances accompanying the offense. Penalties for giving a bribe can include a fine or a prison sentence from up to 2 years or both. In aggravating circumstances when a bribe is given to commit an illegal act, the penalty can be from 4 to 7 years. The definition of a public official includes foreign public officials and employees of International Organizations and Courts for purposes of such offenses as accepting a bribe, giving a bribe and trading in influence. Georgia,s legislation does not allow a local company to deduct a bribe to a foreign official from taxes. White collar crimes such as bribery fall under the investigative jurisdiction of the Prosecutor's Office.

The Government,s September 2005 Anti-Corruption Strategy calls for an effective state management system and legal and public feedback mechanisms to prevent corruption. Among the goals of the strategy are the identification and analysis of conditions conducive to corruption as well as elaboration of mechanisms for their eradication, strengthening of principles of accountability and public disclosure in the public sector, prosecution of lawbreakers and facilitation of competitive development of the business sector.

According to the World Bank,s &Anti-Corruptin in Transition 38 report, Georgia topped the list of transitional countries in terms of anticorruption efforts. The report reviewed the 2002-2005 time period and concluded that Georgia saw the largest reduction in corruption among all transition countries. The World Bank points out that strong leadership in Georgia was the driving force behind the swift and thorough reforms that significantly reduced corruption after 2002. The leadership has taken bold actions to lessen the burden of the state on the economy, improve

fiscal transparency, and strengthen oversight of institutions, all of which has contributed to the decline in corruption.

Georgia also significantly improved in Transparency International's annual Corruption Perceptions Index, moving up from 99th place in 2006 to 79th in 2007, and to 67th in 2008 out of 180 countries surveyed. The Index ranks countries in terms of the degree to which resident and non-resident businesspeople and country analysts perceive corruption to exist in the public and political sectors. Since the Rose Revolution, Georgia's score has steadily improved. Current ranking means that Georgia (3.9 score) has moved out of the group of countries considered to have a "rampant corruption problem" (those under 3.0). In comparison with countries of the former Soviet Union, Georgia ranks well ahead of neighboring Azerbaijan (158) and Armenia (109), Russia (147), as well as Ukraine (134) and Kazakhstan (145).

Georgia reasserted central control over the Black Sea region of Adjara in May 2004, reducing illicit economic activity there. Control of contraband smuggled through South Ossetia has improved, however the Georgian government has raised concerns with Russia and with the international community about continued high levels of smuggling, money laundering, and even counterfeiting of U.S. dollars in the areas outside its control.

Georgia is not a signatory to the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. Georgia has not yet signed the UN Anti Corruption Convention. The latter is on the agenda of the Anti-Corruption Action Plan developed by the government. The Ministry of Justice is analyzing Georgian legislation in order to ensure its compatibility
QGeorgian legislation in order to ensure its compatibility
with the UN convention. Georgia is expected to join the UN convention earlier than the OECD Convention.

Georgia cooperates with GRECO (Group of States Against Corruption) and the OECD,s Anti-Corruption Network for Transition Economies (ACN). GRECO concluded in 2006 that Georgia had successfully implemented reforms to implement the first round of its anti-corruption recommendations. In 2003, ACN proposed an anti-corruption action plan and 21 recommendations for Georgia. In 2006, the OECD positively assessed the progress of anti-corruption measures, and considered all but four of its recommendations implemented.

Bilateral Investment Agreements

Georgia has negotiated bilateral agreements on investment promotion and mutual protection with 26 countries, including the U.S., Armenia, Austria, Azerbaijan, Belgium, Bulgaria, China, Egypt, France, Germany, Greece, Iran, Israel, Italy, Kazakhstan, Kyrgyzstan, Latvia, Moldova, Netherlands, Romania, Turkey, Turkmenistan, Uzbekistan, the United Kingdom, Ukraine, Lithuania and Finland. Internal procedures have been completed and drafts are being negotiated with the governments of India, Bangladesh, Croatia, Denmark, Norway, Philippines, Cyprus, Indonesia, Malta, Czech Republic, and Iceland. Ongoing consultations are being held with Belarus, Tajikistan, Slovenia, Estonia, Slovakia, Sweden, Bosnia-Herzegovina, Switzerland and Jordan. In 2007, Georgia signed a Trade and Investment Framework Agreement (TIFA)with the United States.

A free trade agreement is in force with the Commonwealth of Independent States, and others exist bilaterally with Ukraine, Russia, Kazakhstan, Azerbaijan, Armenia, Moldova, Turkmenistan and Turkey. An agreement is signed, but not yet ratified, with Uzbekistan. Ongoing consultations are being held with the European Union, Belarus, Kyrgyzstan, Cooperation Council of Gulf Arab States and Tajikistan.

OPIC and Other Investment Insurance Programs
From 1993 through 2007, OPIC has committed over $104 million

in financing and political risk insurance to projects in Georgia. Projects supported include the development of hotel and office space, production of pharmaceuticals, food processing and farming, cold storage, banking, mortgage lending, and financial leasing services. In FY 2007, there were two new OPIC loan commitments in Georgia, amounting to $11.3 million. However, in 2008, as part of the USG response to help Georgia recover from the August conflict with Russia, OPIC committed USD 176 million in financing. A large portion of OPIC,s assistance will be used to underwrite mortgages aimed at allowing Georgian banks to offer smaller more affordable mortgages to the Georgian public. Other funding will support commercial and residential property development projects.

Labor

Georgia offers an abundant supply of skilled and unskilled labor at attractive costs compared not only to Western European and American standards, but also to Eastern European. The labor force is among the best educated and most highly trained in the former Soviet Union. While some of the best qualified professionals and technicians emigrated from Georgia (mostly to Russia, the U.S., and Europe) after the Soviet Union's collapse, many have remained in the country or returned from abroad and are attempting to find a new role in a market economy. Unemployment remains high and job creation has been a particular challenge.
The labor market in Georgia is one of the world's freest. Wage negotiations take place between employees and employers, and trade unions are not powerful. Labor, health and safety laws are not considered an impediment to investment. A new labor code which entered into force in June 2006 considerably liberalized labor regulations. The code defines the minimum age for employment (16), work hours (41 per week), annual leave (24 calendar days) and leaves the rest to be regulated by agreement between the employer and employee.

Payment of at least one month,s salary is required if the employer initiates a dismissal. Employees must give one month,s notice of intention to quit. No notice requirement is imposed on the employer prior to dismissal. Employees are entitled to up to 126 days (4 months) of maternity leave, and together with unpaid leave, up to 16 months. Under the new Labor Code, a contract of employment may bar an employee from
QLabor Code, a contract of employment may bar an employee from
using the knowledge and qualifications obtained while performing his duties with another employer. This provision may remain in force even after the termination of labor relations.

Starting from January 1, 2008, employers are no longer required to pay social security contributions for employees. The former 12 percent income tax paid by employees and 20 percent social security tax paid by employers on their employees' wages was merged into a unified personal income tax at the rate of 25 percent in 2008, shifting the employer's tax burden to the employee. From January 2009, the overall effective tax rate paid by both self-employed persons and employees has been further reduced from 25 percent to 20 percent. The state social security system provides modest pension and maternity benefits. The minimum monthly pension is USD 52, and the government is planning to increase it. The average monthly salary in the third quarter of 2008 was GEL 854 (USD 520) for government employees and GEL 560 (USD 337) for private sector employees. The minimum wage for government employees is GEL 115 (USD 69) per month. The minimum wage in the private sector has not changed in many years at GEL 20 (USD 12) per month, but few if any workers earn so little.

Georgia has signed multiple ILO agreements, including the Forced Labor Convention of 1930; the Paid Holiday Convention of 1936; the Anti-Discrimination (employment and occupation) Convention of 1951; the Human Resources Development Convention of 1975; the Right to Organize and Collective Bargaining Convention of 1949; the Equal Remuneration Convention of 1951; the Abolition of Forced Labor Convention

of 1957; the Employment Policy Convention of 1964; and the Minimum Age Convention of 1973.

Foreign Trade Zones/Free Ports

In June 2007 the Parliament of Georgia adopted a law on free industrial zones, which sets forth the terms for forming and functioning of free industrial/economic zones in the country. Financial operations in such zones may be performed in any currency, and foreign companies operating in free industrial zones will be exempt from taxes on profit, property and VAT. Georgia,s Ministry of Economic Development has allocated a 400 hectare area adjacent to the Black Sea Port of Poti for the first such zone. RAK Investment Authority (Rakeen group) became the owner of 100 percent share of LLC Poti Sea Port. The UAE-based company pledged to develop a free economic zone on 300 hectares of land in Poti and to build a new port terminal on a 100 hectare site. Rakeen plans to accomplish its ambitious project within four years and turn Poti Seaport into an international industrial zone with port, railroad and other facilities.

Foreign Direct Investment Statistics

Foreign Direct Investment (FDI) in Georgia peaked several times. In 1997-1998 and 2003-2004, peaks were related to the construction of the Baku)Supsa and Baku-Tbilisi-Ceyhan pipelines. However, despite completion of the pipelines, foreign investment inflows in 2006 -2007 were larger than ever before, due to privatization of state owned enterprises and the impact of economic reforms. The total volume of FDI in Georgia in 2006 USD 1.1 billion (13 percent of GDP) and it increased 197 percent over the 2005 figure. FDI inflows in 2007 were $2,014,842,000. FDI flow in the first half of 2008 once again proved the viability of Georgia,s economic potential. However, the August 2008 conflict with Russia undermined investor confidence, and the subsequent world credit crisis further restricted the inflows of FDI. Despite these challenges, more than USD 3 billion flowed into Georgia in first three quarters of 2008 (81 percent more than in 2007), but in the fourth quarter, FDI inflows slowed to a trickle. Much of the recent investment has been in the real estate and banking sectors.

Official statistics on Foreign Direct Investment (FDI) inflows during recent years are as follows:

2000	-	USD 131,232,000
2001	-	USD 109,840,000
2002	-	USD 167,362,000
2003	-	USD 339,393,000
2004	-	USD 497,827,000
2005	-	USD 449,786,000
2006	-	USD 1,091,100,000
2007	)	USD 2,014,842,000
2008 (Q1-3)	)	USD 3,655,001,000

Breakdown of investments by major countries (USD 1,000,s):

-	2005	2006	2007	2008 (1-3 Q)
Total	449,785	1,190,375	2,014,842	3,655,001
UK	132,925.8	186,824.1	145,474.8	465,224.7
USA	15,025.6	182,651.5	84,412.2	282,089.3
Kazakhstan	0.0	152,310.5	88,486.2	240,796.7
QKazakhstan	0.0	152,310.5	88,486.2	240,796.7
Turkey	21,812.5	129,727.8	93,871.1	245,411.4
Norway	23,620.9	77,894.8	34,200.1	135,715.8
Azerbaijan	66,920.2	77,804.5	41,368.1	186,092.8
Italy	22,833.5	47,219.1	15,228.1	85,280.7
Cyprus	47,537.3	40,071.2	148,643.6	236,252.2
Russia	38,737.6	34,210.0	88,996.5	161,944.2
France	14,383.3	17,221.7	43,726.0	75,331.0
UAE	280.5	422.6	130,858.7	131,561.9
Denmark	319.0	42,477.8	158,126.2	200,923.0
Netherlands	492.0	18,530.2	299,277.2	318,299.3
Czech	1,279.6	15,032.2	227,926.4	244,238.2
Japan	16,610.1	34,433.1	34,368.3	85,411.5

Virgin Isle 4,900.2   129,727.8   187,815.5   322,443.6

Breakdown of investments by economic sectors (USD 1,000,s):

-	2007	2008 (I-III Q)
Total	2,014,842	1,105,420
Agriculture/Fishing	15,527.9	13,256.8
Industry	398,240,9	150,868.3
Energy	362,581.1	165,290.8
Construction	171,891.8	51,998.1
Transport/Communication	416,694.7	312,813.4
Real Estate	30,543.9	149,757.0
Financial Intermediation	136,914.5	73,578.0
Other Services	382,806.6	182,924.2
Other	99,640.2	4,933.2

The UK tops the list of foreign investor countries. Its share in total investments of 2008 three quarters was up to 12.7 percent compared to 7 percent in 2007. The next largest investors were the Netherlands (USD 318 million), the USA (USD 282 million), Turkey (245 million)and Czech Republic (244 million).

The U.S. has been one of the largest foreign investors in Georgia since 1999. In 2000, U.S. investors accounted for 30 percent of FDI in Georgia; in 2001 for 25.7 percent of FDI, which increased in 2002 to 49 percent. In 2003 and 2004 the U.S. share decreased to 21 and 16 percent respectively and dropped to 4.1 percent in 2005. The decline can be attributed to the completion of large pipeline projects as well as increased inflow of capital from other countries. In 2006, U.S investment still accounted for 16.7 percent of the total, but was only 4.1 percent in 2007, and 7 percent in the first 3 quarters of 2008.

Other notable trends include increase in United Arab Emirate,s interest in Georgia, evident in the investments of the Rakeen and Dabi Groups in the port, real estate, banking and other sectors. Source: Statistics Department of Georgia.)
End Text.
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